Supreme Court, U.S.
FILED

961669 APR 18 1997

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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

PADDOCK PUBLICATIONS, INC.,

Petitioner,

v.

CHICAGO TRIBUNE COMPANY, CHICAGO SUN-TIMES, INC., NEW YORK TIMES SYNDICATION SALES CORPORATION, LOS ANGELES TIMES/WASHINGTON POST NEWS SERVICE, INC., TRIBUNE MEDIA SERVICES, INC., CREATORS SYNDICATE, KING FEATURES SYNDICATE, INC., TIMES MIRROR COMPANY d/b/a LOS ANGELES TIMES SYNDICATE, UNITED MEDIA, and UNIVERSAL PRESS SYNDICATE,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the Court of Appeals erred by creating an unprecedented rule of *per se* legality under Section 1 of the Sherman Act for vertical exclusive licensing contracts?

2. Whether the Court of Appeals' decision conflicts with decisions of this Court and other Circuits applying the Rule of Reason to vertical contracts?

3. Whether the Court of Appeals erred by holding that this Court's decision in *FTC v. Motion Picture Advertising Service Co.*, 344 U.S. 392 (1953), is no longer valid authority and does not apply to this case?

4. Whether the Court of Appeals erred by affirming dismissal under Rule 12(b)(6), F.R.Civ.P., on the basis of factual suppositions that directly contradict the allegations of the complaint and the record evidence developed during discovery?

PARTIES TO THIS PROCEEDING

The caption of this case contains the names of all the parties to this proceeding. Petitioner Paddock Publications, Inc. does not have a parent corporation or any subsidiaries.

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PETITION FOR A WRIT OF CERTIORARI

Paddock Publications, Inc. ("Paddock") hereby petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The panel opinion of the Court of Appeals (App. 12) is reported at 103 F.3d 42 (7th Cir. 1996). The order of the Court of Appeals (App. 13) denying the petition for rehearing and suggestion of rehearing en banc is unreported. The two opinions of the District Court (App. 61-89, 90-92) and the Magistrate Judge's Report and Recommendation (App. 14-60) are unreported.

JURISDICTION

The judgment of the Court of Appeals was entered on December 16, 1996. A timely petition for rehearing and suggestion of rehearing en banc was denied on January 21, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, provides in pertinent part that:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States . . . is declared to be illegal . . . .

STATEMENT OF THE CASE

Paddock, the publisher of a daily newspaper, the Daily Herald, in Chicago's northwest suburbs, brought this injunctive action under the federal antitrust laws to break the exclusive stranglehold that its competitors, the Chicago Tribune and Chicago Sun-Times, have on the nation's leading news services and features in the Chicago newspaper market. The Tribune and Sun-Times have long dominated the sale of newspapers in the Chicago area and use that market power to demand that the New York Times News Service ("NYT News Service") and the Los Angeles Times/Washington Post News Service ("LAT/WP News Service") and all the leading feature syndicators give them exclusive licenses that last as long as the Tribune and Sun-Times want them. Paddock cannot obtain news services and features of the quality and popularity that would enable it to compete with the Tribune and Sun-Times. (App. 94-99, 102-106, 109-111, 115-120, 123-130, 132-136, 159-160, 194-196, 241-242.)

The Tribune and Sun-Times require these exclusive licenses for the specific purpose of blocking Paddock and other smaller newspapers from obtaining vital resources that are available to hundreds of newspapers across the country. The effect on competition is intended and clear: Paddock and other papers cannot mount a challenge to the Tribune's and Sun-Times' dominance because most newspaper readers insist on the comprehensive national and international coverage that the NYT News Service and LAT/WP News Services uniquely provide, as well as the popular comics and columns that have national prominence. The Tribune and Sun-Times have concededly enforced their exclusive licenses to prevent their

readers from switching to other papers, including the Daily Herald. Consequently, Paddock has not been able to expand its circulation significantly outside the northwest suburbs where the Daily Herald originated. Consumers in the Chicago area are denied the choice, quality, and lower prices that greater competition would provide. (App. 104-106, 109-111, 126-130, 132-136, 145-147, 152, 160-161, 254, 259.)

The exclusive licenses provide no benefits to competition or consumers. If other newspapers had access to the vital news services and features—which the Tribune and Sun-Times did not create or develop but buy off the shelf—the quality of the Tribune and Sun-Times would not suffer because they could still offer the same news service articles and features that they now provide. However, without these restrictive exclusive arrangements, Paddock and other newspaper publishers could offer better products to consumers. (App. 106-107, 110-111, 130, 134-136, 145-147, 153, 156-158, 164-165, 173-174, 196.)

Decisions Below

The Magistrate Judge's Recommendation. The Magistrate Judge concluded that Paddock's claims under Section 1 of the Sherman Act should be dismissed because the antitrust laws do not reach separate but parallel exclusive contracts entered into by the dominant firms in a market even if in the aggregate they injure competition. (App. 58-60.) However, the Magistrate Judge also concluded that the defendants' alternative summary judgment motion should be denied because the facts are disputed with respect to the exclusive licenses' effects on competition and the defendants' contentions that the

exclusives are justified. (App. 21, 24-25, 43, 46-53.) The Magistrate Judge rejected the defendants' contention that the exclusive licenses are merely distribution contracts through which the newspapers resell the news service material and features to consumers. The Magistrate Judge concluded instead that "[r]educing the number of newspapers implicates consumer welfare in a way in which reducing the number of distributors of a product would not." (App. 37-40.)

District Court Dismissal. The District Court concluded that Section 1 of the Sherman Act cannot be violated by the collective anticompetitive effect of two dominant firms' exclusive contracts if those firms have not conspired. The Court refused to follow *FTC v. Motion Picture Advertising Service Co.*, 344 U.S. 392 (1953), even though this Court held that four non-conspiring firms' separate exclusive license contracts violated the antitrust laws because of their aggregate anticompetitive effects. (App. 68-78.) The District Court did not consider Paddock's claims under the Rule of Reason. (App. 85 n.13.)

The District Court granted Paddock leave to amend, but dismissed the Amended Complaint on the ground that Paddock was still attempting to "manufacture an antitrust violation" by combining the Tribune's and Sun-Times' exclusive licenses to establish a restraint of trade. (App. 91-92.)

The Court of Appeals' Decision. Paddock appealed under 28 U.S.C. § 1291 from the final judgment dismissing its case under Rule 12(b)(6). The Court of Appeals affirmed the dismissal. The Seventh Circuit held, as a matter of law, that there could be no injury to competi-

tion in this case because the defendant news services and features syndicators had entered into the exclusive contracts with the Tribune and Sun-Times independently to maximize their profits. (App. 3-6.) In the Court's view, the exclusive licenses helped maintain vigorous competition in the Chicago newspaper market; there were numerous other news services and features available to the Daily Herald; and the exclusive licenses were open on short notice to rebidding by the Tribune's and Sun-Times' competitors. (App. 5, 6, 12.) The Court did not mention the complaint's well-founded allegations that the exclusive licenses had harmed competition and consumers in the Chicago newspaper market. The Court rejected Paddock's reliance on *Motion Picture Advertising* because that decision was deemed to be based on an outdated mode of antitrust analysis. The Seventh Circuit also found *Motion Picture Advertising* to be limited to Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), and Justice Douglas' statement in the majority opinion that the Sherman Act had been violated was characterized as "unreasoned dictum." (App. 7-11.)

Paddock sought rehearing en banc because the panel's opinion ignored the Rule of Reason and adopted an unprecedented rule of *per se* legality on factual assumptions contrary to the complaint's allegations. Rehearing was denied without comment. (App. 13.)

REASONS FOR GRANTING THE PETITION

I. THE SEVENTH CIRCUIT ADOPTED AN UNPRECEDENTED RULE OF PER SE LEGALITY FOR EXCLUSIVE VERTICAL SUPPLY CONTRACTS

Paddock has alleged all the elements of a violation of the Rule of Reason: exclusive contracts between newspapers with market power and suppliers that block those newspapers' competitors from access to vital supplies, thereby seriously impeding competition and harming consumers by denying them the benefits of greater product choice and quality and lower prices. Nevertheless, the Court of Appeals affirmed dismissal under Rule 12(b)(6), holding that under no set of facts could such licenses violate Section 1 of the Sherman Act. This result overturns decades of antitrust precedent.

The Seventh Circuit did not even mention the Rule of Reason, which this Court held in *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 58-59 (1977), governs claims under Section 1 of the Sherman Act against vertical arrangements. Judge Easterbrook, the author of the Seventh Circuit's opinion, has long criticized the Rule of Reason because it prescribes a supposedly "empty" balancing test of anticompetitive and pro-competitive factors. Frank H. Easterbrook, *The Limits of Antitrust*, 63 Tex.L.Rev. 1, 11-14 (1984).

Judge Easterbrook has proposed that courts adopt certain presumptions, or "filters," to determine whether particular antitrust claims should be dismissed. *Id.* at 14-15. The rationale for these filters is skepticism that litigation can reach correct economic results: ". . . it is fantastic to suppose that judges and juries could make

such an evaluation" of the costs and benefits of a particular practice. *Id.* at 11. The result is rough justice: "If presumptions let some socially undesirable practices escape, the cost is bearable." *Id.* at 14.

These views have now become Seventh Circuit law, and they are not limited to the vertical exclusive licenses specifically at issue in this case. All vertical arrangements are deemed to be "usually procompetitive." Frank H. Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 Antitrust L.J. 135, 168 (1984). "They are all the same." *Id.* at 135.

The Seventh Circuit's holding of *per se* legality for supposedly profit-maximizing vertical contracts is unprecedented.[1] "Mere invocation of possible pro-competitive purposes will not suffice to legalize a restraint under the rule of reason." *Graphic Products Distributors, Inc. v. Itek Corp.*, 717 F.2d 1560, 1573 n. 22 (11th Cir. 1983). As this Court recently explained:

> Legal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored in antitrust law. This Court has preferred to resolve antitrust claims on a case-by-case basis, focusing on the "particular facts disclosed by the record."

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[1] The Seventh Circuit cited no authority for its holding that profit-maximizing is a defense to an antitrust claim. *See United States v. General Motors Corp.*, 384 U.S. 127, 142 (1966) (fact that each party acted in pursuit of its "lawful interest" not a defense under Section 1). All restraints of trade are designed to make more money for the parties entering into them.

Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 466-467 (1992) (*quoting Maple Flooring Mfrs. Assn. v. United States*, 268 U.S. 563, 579 (1925)).

Such a fundamental change in antitrust law should not be allowed without a full hearing in this Court.

II. THE SEVENTH CIRCUIT'S DECISION CONFLICTS WITH THE DECISIONS OF THIS COURT AND OTHER CIRCUITS

This Court has never departed from its holding in *Sylvania* that non-price vertical arrangements are to be judged under the Rule of Reason. *See Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 724 (1988). Other Circuits continue to apply the Rule of Reason to vertical cases like this one. *See Orson, Inc. v. Miramax Film Corp.*, 79 F.3d 1358 (3d Cir. 1996); *Retina Associates, P.A. v. Southern Baptist Hospital*, 105 F.3d 1376 (11th Cir. 1997); *American Ad Management, Inc. v. GTE Corp.*, 92 F.3d 781, 789 (9th Cir. 1996); *U.S. Healthcare, Inc. v. Healthsource, Inc.*, 986 F.2d 589, 595-597 (1st Cir. 1993).

In *Orson*, the plaintiff movie theater challenged exclusive licenses held by a competing theater to a leading movie distributor's films. The Third Circuit explained the standard approach to deciding such cases under Section 1 of the Sherman Act:

> Whether a business arrangement unreasonably restrains trade is determined by the courts, on a case-by-case basis, using a rule of reason which considers all relevant factors in examining a defendant's purpose in implementing the restraint and the restraint's effect on competition.

Orson at 1367. The Rule of Reason is applied through shifts in the burden of proof as evidence is presented. Initially, the plaintiff bears the burden of proving either actual anticompetitive effects or its surrogate, market power. If the plaintiff makes that showing, the burden shifts to the defense to establish sufficient pro-competitive effects. The plaintiff may then rebut by demonstrating that the restraint is not "reasonably necessary" to achieve those pro-competitive effects. *Id.* at 1367-1368. *See also* VII Phillip E. Areeda, Antitrust Law ("Areeda") ¶ 1507b (1986).

If the Rule of Reason were applied in this case as it was in *Orson*, Paddock would be entitled to a trial, not dismissal under Rule 12(b)(6). Since Paddock has sufficiently alleged the elements of a Rule of Reason violation, defendants' motion to dismiss should have been denied.[2] Unlike the plaintiff in *Orson*, 79 F.3d at 1372, Paddock has submitted substantial evidence that it does not have access to "alternative sources of supply" that would enable it to compete effectively with the Tribune and Sun-Times. Indeed, the Magistrate Judge concluded that Paddock's evidence created disputed factual issues with respect to the justifications for the exclusives

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[2] The Seventh Circuit's facile conclusion (App. 5) that this case should be viewed as an "essential facility" case without an essential facility does not excuse its failure to apply the Rule of Reason. Paddock never made a claim under the essential facility doctrine, but has always claimed that the exclusive licenses violate the Rule of Reason. "[T]he same competitive practice may be reviewed under several different rubrics and a plaintiff may prevail by establishing a claim under any one of them." *U.S. Healthcare, Inc.*, 986 F.2d at 593.

offered by the defendants, thereby defeating the defendants' alternative motion for summary judgment. (App. 21, 24-25, 43, 46-53.) The Court of Appeals simply rewrote the record to fit the economic assumptions for its rule of *per se* legality.

The Seventh Circuit's substitution of a *per se* rule of legality for the Rule of Reason in cases involving vertical supply arrangements under Section 1 of the Sherman Act is unwarranted, in conflict with the decisions of this Court and other Circuits, and must be reversed.

III. THE SEVENTH CIRCUIT ERRED BY REFUSING TO FOLLOW THIS COURT'S DECISION IN *MOTION PICTURE ADVERTISING SERVICE*

In defending its new *per se* rule, the Seventh Circuit rejected this Court's decision in *Motion Picture Advertising Service Co.* The defendant in that case was found to have violated Section 1 of the Sherman Act because it and three other major firms together holding 75% of the market had, without conspiring, used similar exclusive-dealing contracts that substantially foreclosed competition by other firms. Characterizing *Motion Picture Advertising* as a "derelict" and "antique antitrust opinion," the Seventh Circuit discarded the statement in Justice Douglas' majority opinion that Section 1 was violated as "unreasoned dictum." (App. 9.) The Seventh Circuit departed from its own decisions requiring antitrust decisions of this Court to be followed even though there is some reason to question whether this Court would still view them as valid precedents. *See, e.g., Khan v. State*

Oil Co., 93 F.3d 1358, 1362-1364 (7th Cir. 1996), *cert. granted in part*, ___ U.S. ___, 117 S.Ct. 941 (1997).[3]

Motion Picture Advertising is not the "derelict" and "antitrust antique" depicted by the Seventh Circuit. While the Seventh Circuit criticized *Motion Picture Advertising* because the analysis in that case "depends on 'foreclosure' of sales to competitors without proof of injury to consumers" (App. 8), the "foreclosure" approach followed in *Motion Picture Advertising* is still good law. Justice O'Connor's concurring opinion in *Jefferson Parish Hospital Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984), used the same foreclosure approach as *Motion Picture Advertising*:

> Exclusive-dealing arrangements may, in some circumstances, create or extend market power of a supplier or the purchaser party to the exclusive-dealing arrangement, and may thus restrain horizontal competition. Exclusive dealing can have adverse economic consequences by allowing one supplier of goods or services unreasonably to deprive other suppliers of a market for their

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[3] The Seventh Circuit alternatively attempted to distinguish *Motion Picture Advertising* by relying on facts that are contrary to both Paddock's complaint and the record evidence: that this case involves exclusive distributorships rather than the type of exclusive dealing contracts at issue in *Motion Picture Advertising*, and that the contracts here are open for renegotiation and bidding on "short notice." (App. 12.) As demonstrated below, the exclusive licenses involved in this case are not distributorships but exclusive supply contracts, and the exclusive licenses will continue as long as the Tribune and Sun-Times want them. At the very least Paddock should have the opportunity to present evidence refuting these supposedly distinguishing facts.

> goods, or by allowing one buyer of goods unreasonably to deprive other buyers of a needed source of supply. In determining whether an exclusive-dealing contract is unreasonable, the proper focus is on the structure of the market for the products or services in question—the number of sellers and buyers in the market, the volume of their business, and the ease with which buyers and sellers can redirect their purchases or sales to others. Exclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal. (Emphasis added.)

The 1992 summary of antitrust law by the Antitrust Section of the American Bar Association, Antitrust Law Developments (3d ed. 1992) Vol. I, at 176-177 (footnotes omitted), also focuses on the extent of market foreclosure:

> If an arrangement is viewed as exclusive dealing, the courts and the Commission have considered a number of factors in applying a rule of reason analysis. Perhaps most important is the percentage of the market foreclosed. As the percentage of the market foreclosed rises beyond 20% to 30%, the probability that a violation will be found increases.

Market foreclosure created by exclusive supply contracts controlled by firms with market power prevents other competitors from entering the market or expanding their market penetration and thereby injures consumers. *See* VIII Areeda ¶ 1652c1 at 571-573 (describing anticompetitive effects in the "upstream" market of exclusive supply contracts held by dominant firm). In this case, consumers are hurt by having a restricted choice of

newspapers, by being deprived of the improvement in the quality of their papers that greater competition would inspire, and by paying higher prices for the limited number of papers available to them. Output is restricted and prices are increased, the hallmarks of anticompetitive effects and consumer injury. *See NCAA v. Bd. of Regents of Univ. of Okla.*, 468 U.S. 85, 99-100 (1984).

The Seventh Circuit also agreed with the District Court that, in the absence of a conspiracy between them, the Tribune's and Sun-Times' exclusive licenses could not properly be aggregated to assess their harmful effects on competition. (App. 8.) To the contrary, this Court in *Motion Picture Advertising*, in determining that the defendant had violated the Sherman Act, considered the fact that the other three major firms in the market used similar exclusive contracts even though there was no contention that the firms had conspired. The Seventh Circuit's decision to ignore industry practices demonstrates again its aversion to the Rule of Reason in which all such market facts must be evaluated. The law, at least prior to the Seventh Circuit's decision, was that:

> The character of the market(s) in which the parties operate, their market shares, and the behavior and shares of their rivals determine whether a possible threat to competition has or will come to pass and whether any such impact is likely to be significant.

VII Areeda ¶ 1503b, at 376.

This Court explained in *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 768 (1984), that vertical arrangements may violate Section 1 under the Rule of Reason even if they do not "threaten[ ] monopolization."

The Seventh Circuit's rejection of *Motion Picture Advertising*, however, entails that vertical arrangements violate the Sherman Act only if there is a horizontal agreement between the firms using the same practice or one of the firms achieves a monopoly. In other words, the Rule of Reason for vertical arrangements becomes a dead letter. Rather than merely refusing to follow a supposedly out-dated precedent, the Seventh Circuit's decision would invalidate an entire body of antitrust law judging vertical arrangements under the Rule of Reason.

IV. THE SEVENTH CIRCUIT VIOLATED RULE 12(b)(6) BY RESTING ITS DECISION ON FACTUAL PRESUPPOSITIONS AT ODDS WITH THE CRUCIAL ALLEGATIONS OF THE COMPLAINT

The Seventh Circuit's ultimate holding is that vertical exclusive licenses are *per se* legal; the facts of a particular case do not matter. To justify that conclusion, however, the Seventh Circuit ignored the allegations of Paddock's complaints and relied on factual presuppositions unsupported by the record. Indeed, the Seventh Circuit's opinion is contradicted by the evidence submitted by Paddock in opposition to the defendants' alternative summary judgment motion. The decision below flouts the liberal federal civil pleading rules, *Leatherman v. Tarrant County Narcotics Intelligence and Coordination Unit*, 507 U.S. 163 (1993), and the longstanding practice under Rule 12(b)(6) of assuming the truth of the complaint's allegations in deciding whether a valid cause of action is stated. "What Rule 12(b)(6) does not countenance are dismissals based on a judge's disbelief of a complaint's factual allegations." *Neitzke v. Williams*, 490 U.S. 319, 327 (1989).

The Seventh Circuit's factual presuppositions that conflict with the record are graphically portrayed by the table on the next two pages and fully documented in the following pages. Such violent revision of the record cannot be countenanced under Rule 12(b)(6).

	Court of Appeals' Factual Assumptions	Paddock Complaint Allegations	Evidence
A.	The exclusive licenses create a "vigorous market" that would be damaged if competing papers ran the same stories and features. (App. 6.)	The exclusive licenses are barriers preventing new papers from entering the market and the Daily Herald from expanding its circulation. (App. 95, 101, 110, 116, 128, 134-136.)	Tribune editor testifies that decline in number of competitors has created less incentive for Tribune to use its own original material. (App. 250-251.) Magistrate Judge concludes that end of exclusives would enhance competition with each newspaper using its own staff's work. (App. 47-48.)
B.	Many quality comics and other news services are available to Paddock. (App. 3, 5.)	Paddock does not have access to other news services and features of comparable quality and popularity that would enable it to compete with the Tribune and Sun-Times. (App. 95, 102-105, 109-110, 116, 123-128, 133.)	Paddock's journalism expert concludes that there are no available news services and features comparable to those controlled exclusively by the Tribune and Sun-Times. (App. 194-196.)
C.	Seventh Circuit stresses Paddock's concession that the news services	Paddock makes no such concession and instead alleges that	Magistrate Judge finds facts disputed on defendants' contention

	and features syndicators use exclusives because "it is the most profitable way to do business." (App. 4.)	Tribune's and Sun-Times' market power enable them to demand exclusivity. (App. 101, 106-107, 112, 122-123, 126, 130.)	that exclusives allow licensing revenues to be maximized. (App. 50-53.) Syndicators have made at least as much money in markets where exclusivity has been broken. (App. 203-207, 221-227.)
D.	Seventh Circuit concludes that licenses are open on short notice to highest bidder. (App. 12.)	Paddock alleges that the exclusives last as long as the Tribune and Sun-Times want them. (App. 104-105, 127.)	Syndication witnesses testify that the licenses are not put up for renegotiation or bidding when formal terms expire. (App. 202, 210-213, 216-220, 228-230, 243-249.) NYT News Service President testifies it would not license Paddock at any fee. (App. 271.)
E.	Seventh Circuit depicts Tribune and Sun-Times as mere distributors of news service material and features. (App. 9-10.)	Paddock alleges that the news services and features are vital resources that newspapers use in creating their distinctive products. (App. 95, 100, 105, 110-111, 121, 129.)	Magistrate Judge rejects defendants' contention that newspapers are mere distributors of the licensed material. (App. 35-40.)

A. The Supposed Creation of a "Vigorous Market" through the Exclusives. The Seventh Circuit justified dismissal of Paddock's case by stating that the exclusive licenses in question create a "vigorous market" that would be damaged if competing newspapers could publish the same stories and features. (App. 6.) But Paddock has alleged that the exclusive licenses are barriers preventing new papers from entering the market and the Daily Herald from expanding its circulation. (App. 95, 101, 110, 116, 128, 134-136.)

The Seventh Circuit's depiction of a "vigorous market" in which exclusives provide incentives to originality is contrary to the evidence of record. A Tribune editor testified that, with the decline of competition in the Chicago newspaper market, the Tribune's desire to use its own staff-generated material whenever possible has "eroded" and it now uses more Associated Press stories that are available to all papers:

> I think that in the era when there were four, six or eight newspapers in Chicago, there was great—people placed great stock in having a maximum amount of staff-generated copy. But as I said, I don't think that that's a valid model any more. [App. 250-251.]

The Magistrate Judge made the same point in concluding that it is "pure speculation" whether exclusive licensing promotes competition. (App. 50.) If there were no exclusives, the newspapers would still compete through their "selection and editing" of the licensed material, and competition would be "enhanced" as the newspapers placed greater stress on their own original work. (App. 47-48.)

The Magistrate Judge's finding of possible injury to competition and consumer welfare is also diametrically opposed to the Seventh Circuit's opinion:

> . . . Paddock has alleged an impediment to competition; any smaller third paper attempting to compete in the Chicago metropolitan market with the Chicago Tribune and Chicago Sun-Times will come up against the same obstacle of exclusive licenses. . . .
>
> . . . [D]rawing reasonable inferences in Paddock's favor, it appears that exclusive licenses are a significant barrier to entry and may serve no useful purpose other than maintaining the duopoly in the Chicago market. [App. 24-25.]

What the Seventh Circuit mischaracterized as a "vigorous market" is in fact a duopoly protected by high market barriers to insure that competition will never be vigorous.

B. The Supposed Availability of Quality News Services and Features to Paddock. The Seventh Circuit cited Paddock's supposed "concession" that the Associated Press, Reuters, and "many quality comics" are available to it and suggested that Paddock merely wants the "best" material. (App. 3, 5.) To the contrary, Paddock has alleged and shown that none of the available news services "is a reasonably effective substitute" for the leading news services, the NYT News Service and the LAT/WP News Service, which are controlled exclusively in this market by the Tribune and Sun-Times. (App. 95, 102, 109-110, 116, 123-124, 133, 194-195.) Paddock has also alleged and shown that the available features are of no use to it in competing with the Tribune and Sun-

Times. (App. 95, 103-104, 109-110, 116, 125-126, 133, 195-196.)

C. The Supposed Profit-Maximizing by Defendant News Services and Syndicators. The Seventh Circuit stated that Paddock concedes that each defendant news service and syndicator uses exclusive licenses because "it is the most profitable way to do business." (App. 4.) Paddock made no such concession and contends to the contrary that the dominant papers have used their market power to demand exclusivity. (App. 101, 106-107, 112, 122-123, 126, 130.) The record evidence shows that the news services and syndicators would earn at least as much if they could license their products non-exclusively to other papers in the same market, and there is no evidence that the Tribune and Sun-Times would abandon popular features if they were licensed non-exclusively. For example, when the San Francisco Chronicle lost exclusivity on certain features, it continued to license those features. The fees it paid to defendant United Feature Syndicate were reduced, but United received fees from additional licensees that made it "roughly a wash." (App. 203-207.) When the Indianapolis Star lost its exclusivity to certain features, the Star continued to license those features and paid the same fees to the syndicator. However, the suburban paper that could now license the features also paid fees to the syndicator, which as a result received higher total fees without exclusivity. (App. 221-227.) In addition, Paddock's economics expert explained the possibility that the exclusives do not maximize the syndicators' profits. (App. 174-175.)

The Magistrate Judge found, contrary to the Seventh Circuit, that the facts are disputed on this issue:

"[A]lthough defendants have raised the justification of maximizing revenues, they have not shown the absence of a genuine issue of material fact. . . ." (App. 50-53.)

D. The Supposition that the Exclusive News Services and Features Are Open for Bidding on Short Notice. One of the key "facts" relied upon by the Seventh Circuit is that Paddock has never tried to out-bid the Tribune and Sun-Times for the leading news services and popular features and that Paddock could obtain them if it agreed to pay more than its competitors. As the Court below put it: "[S]omeone with a better offer can get or sell news on short notice." (App. 12.)

That statement is simply not true. Paddock has alleged that the exclusive licenses to the leading news services and most popular features "are automatically renewed, continue on a perpetual basis, and deny the Daily Herald the opportunity to obtain access to them." (App. 104-105, 127-128.) The evidence establishes that once an exclusive is granted to the Tribune or Sun-Times, that paper will hold that exclusive as long as it wants it.[4] The news services and syndicators do not put their licenses up for re-bidding or even renegotiation when the formal terms

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[4] The Daily Herald normally is not even offered the leading features. They are first offered to the Tribune and then, if the Tribune declines, to the Sun-Times. If both the Tribune and Sun-Times decline a feature, it is then offered to the remaining papers on a non-exclusive basis. If the feature becomes popular, the Tribune or the Sun-Times can still license it. (App. 126-127.) That was the case with the Daily Herald's only popular comic strip, "Dilbert." The Daily Herald licensed it after it was rejected by the Tribune and Sun-Times. Later the Tribune licensed it through an exclusive that blocks access to all papers except the Daily Herald.

of the licenses expire. (App. 202, 210-213, 216-220, 228-230, 243-249.) The president of the New York Times News Service was emphatic: It would not license the Daily Herald at any fee that Paddock would offer to pay. (App. 271.) Paddock has tried to obtain these news services and features, but has been rejected without any suggestion that they would be available if Paddock offered a higher fee than the existing licensees.[5] (App. 157.)

Contrary to the Seventh Circuit's opinion, the effect on competition of an exclusive contract cannot be determined as a matter of law based merely upon the licenses' boilerplate termination provisions. The specific effects of exclusivity must be assessed in each case. *See U.S. Healthcare*, 986 F.2d at 596. Here, Paddock has admissions that the licenses will last as long as the licensing newspaper wants them.

E. The Characterization of Newspapers as Mere Distributors of the News Service Stories and Syndicated Features. The Seventh Circuit adopted the defendants' contention that the Tribune and Sun-Times are simply distributors of the news service material and features that they exclusively license. (App. 9-10.) Paddock alleges instead that the news services and features syndicators provide important inputs that newspapers meld with their own "in-house" material to create a new product. (App. 95, 100, 105, 110-111, 121, 129.)

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[5] In any event, a plaintiff is not required to engage in futile efforts to deal with the alleged antitrust violators in order to state a claim. *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 120 n. 15 (1969); *Continental Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 699-700 (1962).

The District Court agreed with Paddock. The Magistrate Judge rejected the defendants' contention that newspapers are "distributors":

> [I]t is a distortion to speak of newspapers as "distributors" of news and features "manufactured" by the syndicators and news services. . . . Newspaper publishers are not simply resellers, but creators of products in their own right. While news services and syndicates provide important, perhaps necessary ingredients, each newspaper is the sum of its news services, its features, and its own reporting and commentary. [App. 37 (emphasis in original).]

The Tribune does not view itself as a New York Times distributor. The Tribune's editor responsible for acquiring news service and feature licenses stated that the Tribune's product is "the newspaper as a whole"; it does not sell individual features to the public: "They are part of the product." (App. 237.)[6]

Rule 12(b)(6) does not permit the Seventh Circuit to substitute its version of the facts to suit the preconceptions of its economic theory.[7] The Seventh Circuit also

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[6] In fact, the Tribune uses little of the large volume of material provided by the NYT News Service. (See the summary of the survey of the Tribune's news sources by Paddock's counsel at App. 267.) The apparent purpose of the Tribune's exclusive license to that material is to block the Daily Herald from using it.

[7] In addition to the factual presuppositions discussed above, the Seventh Circuit also drew on supposed factual analogies from the automobile, motion picture, and television industries that have no source in the record of this case. (App. 5-6, 11-12.)

failed to honor the cautionary antitrust principle of not creating a new *per se* rule until the effects on competition of the business practice in question are fully understood. *See Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 24 (1979); *White Motor Co. v. United States*, 372 U.S. 253, 263 (1963).

CONCLUSION

The Seventh Circuit has created a new doctrine of *per se* legality for vertical arrangements that will stifle the development of new competition in the newspaper industry as well as other markets in which dominant firms use exclusive contracts to block their competitors from vital supplies. The Seventh Circuit's decision marks a 180-degree turn in antitrust law supplanting the Rule of Reason and this Court's focus on the facts of each case with the doctrine of one school of economics. Paddock's allegations and evidence have never received a hearing to which they are entitled under Rule 12(b)(6) and the law repeatedly applied by this Court.

Therefore, Paddock asks the Court to grant this Petition, set this case for full briefing and argument, and reverse the Seventh Circuit's decision.

Respectfully submitted,

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Dated: April 16, 1997